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13 CFR Part 121

Small Business Size Standards: Revised Size Standards Methodology

AGENCY: U.S. Small Business Administration.

ACTION: Notice of Availability of White Paper on Revised Size Standards Methodology for Comments.

SUMMARY: The U.S. Small Business Administration (SBA or Agency) advises the public that it has revised its white paper explaining how it establishes, reviews and modifies small business size standards. The revised white paper, entitled “Size Standards Methodology (2017),” (Revised Methodology) is available for review and comments on SBA's website at <http://www.sba.gov/size>. The document describes the SBA’s methodology for establishing, reviewing and adjusting its small business size standards pursuant to the Small Business Act (Act) and related legislative guidelines. Under the Act (Public Law 85-536, as amended), the SBA’s Administrator has authority to establish small business size standards for Federal government programs. The white paper provides a detailed description of the size standards methodology. SBA welcomes comments and feedback on the Revised Methodology, which SBA intends to apply to the forthcoming five-year comprehensive review of size standards required by section 1344(a)(2) of the Small Business Jobs Act of 2010 (Jobs Act), Public Law 111-240, Sep. 27, 2010. This notice discusses the comments SBA received on the methodology that was applied to the recent review of size standards under the Jobs Act and Agency’s responses, followed by a description of major changes to the methodology and their impacts on size standards.

DATES: SBA must receive comments to this revised methodology on or before  
[INSERT DATE 60 DAYS AFTER DATE OF PUBLICATION IN THE FEDERAL  
REGISTER].

ADDRESSES: The revised “Size Standards Methodology (2017)” (Revised  
Methodology) White Paper is available on the SBA's website at <http://www.sba.gov/size>.

Comments may be submitted on the Revised Methodology, identified by Docket number  
TBD, by one of the following methods: (1) Federal eRulemaking Portal:

<http://www.regulations.gov>. Follow the instructions for submitting comments, (2)

Mail/Hand Delivery/Courier: U.S. Small Business Administration, Khem R. Sharma,  
Chief, Office of Size Standards, 409 Third Street, SW., Mail Code 6530, Washington,  
DC 20416, or (3) E-mail at [sizestandards@sba.gov](mailto:sizestandards@sba.gov).

SBA will post all comments on [www.regulations.gov](http://www.regulations.gov). If you wish to submit  
confidential business information (CBI) as defined in the User Notice at  
[www.regulations.gov](http://www.regulations.gov), please submit the information to Khem R. Sharma, Chief, Office  
of Size Standards, 409 Third Street, SW., Mail Code 6530, Washington, DC 20416, or  
send an e-mail to [sizestandards@sba.gov](mailto:sizestandards@sba.gov). Highlight the information that you consider to  
be CBI and explain why you believe SBA should hold this information as confidential.  
SBA will review the information and make the final determination of whether it will  
publish the information or not.

CONTACT INFORMATION: Khem R. Sharma, Chief, Office of Size Standards, (202)  
205-7189 or [sizestandards@sba.gov](mailto:sizestandards@sba.gov).

## SUPPLEMENTARY INFORMATION

To determine eligibility for Federal small business assistance programs, SBA establishes small business definitions (commonly referred to as size standards) for private sector industries in the United States. SBA's existing size standards use two primary measures of business size: average annual receipts and number of employees. Financial assets and refining capacity are used as size measures for a few specialized industries. In addition, the SBA's Small Business Investment Company (SBIC), 7(a), Certified Development Company (CDC/504) Programs determine small business eligibility using either the industry based size standards or net worth and net income based alternative size standards. Presently, there are 28 different industry based size standards, covering 1,031 North American Industry Classification System (NAICS) industries and 14 "exceptions." Of these, 531 are based on average annual receipts, 509 on number of employees (one of which also includes barrels per day total refining capacity), and five on average assets.

In 2007, SBA initiated a comprehensive review of size standards. Subsequently, Congress passed the Small Business Jobs Act in 2010 (Jobs Act) (Public Law 111-240, 124 Stat. 2504, Sept. 27, 2010) requiring SBA to review, every five years, all size standards and make necessary adjustments to reflect market conditions. SBA recently completed the first five-year review of size standards under the Jobs Act and will start the next five-year review in the near future. Usually, once every five years, SBA adjusts all monetary based size standards for inflation. The SBA's latest inflation adjustment to size standards became effective on July 14, 2014 (79 FR 33647 (June 12, 2014)).

As part of the comprehensive size standards review initiated in 2007, SBA established a detailed methodology explaining how SBA establishes, reviews and adjusts size standards based on industry and Federal contracting factors. In 2009, SBA published a notice in the Federal Register notifying the public that SBA's "Size Standards Methodology" White Paper (Methodology) is available on the SBA's website at [www.sba.gov/size](http://www.sba.gov/size) for review and comments (78 FR 53940 (October 21, 2009)). Specifically, in the notice and in all subsequent proposed rules revising size standards for various NAICS Sectors, SBA sought comments on a number of issues concerning its Methodology, such as whether there are alternative methodologies that SBA should consider; whether there are alternative or additional factors or data sources that SBA should evaluate; whether SBA's approach to establishing small business size standards makes sense in the current economic environment; whether SBA's applications of anchor size standards are appropriate in the current economy; whether there are gaps in SBA's Methodology because of the lack of comprehensive data; and whether there are other facts or issues that SBA should consider. The comment period for the Methodology was open from October 21, 2009 to September 30, 2015.

SBA also sought comments on a number of policy questions that the Agency has to consider when developing a methodology for establishing, evaluating and revising its small business size standards, such as how high a small business size standard should be, should there be a single measure of business size for all industries (i.e., employees or annual receipts), should there be a fixed number of "bands" of size standards or a separate size standard for each industry, and should employee based size standards be

adjusted to account for labor productivity growth and technology similar to the adjustment of monetary based size standards for inflation.

SBA received 17 comments specifically on its Methodology and many comments addressing the different aspects of the Methodology as applied to various proposed rules on both receipts-based and employee-based size standards. These comments and SBA's responses are discussed below.

### **Comments on Primary Factors**

1. Average size: One commenter noted that the accuracy of the weighted average would increase if the size groupings for higher employment and receipts levels were more refined. A few commenters suggested using the median firm size, rather than average firm size.

SBA's response: SBA agrees, but increasing the number of size groupings for higher employment and receipts levels will increase the amounts of data that will be suppressed for the disclosure restriction. As the number of firms declines with receipts or employment levels in every industry, more granular size groupings would result in only a very few firms in higher size groupings, thereby causing employment and receipts levels to be suppressed to ensure confidentiality. A sizeable number of cells are already suppressed in the existing size groupings, especially at the 6-digit NAICS industry levels that SBA uses as the bases for size standards. When industry data on firm sizes are found or likely to be very skewed, SBA will consider using the median firm size, instead of the average.

2. Start-up costs and entry barriers: One commenter argued that average assets is not a good measure of start-up costs and entry barriers, such as product

differentiation, brand reputations, patents, intellectual property, economies of scale, and the need for specialized capital goods, especially in services industries. Data on asset size are not publicly available for many private companies and, where they are available, the data will not provide useful quantitative information on the magnitude of start-up costs and entry barriers across industries, the commenter added. For these reasons, the commenter recommended that SBA should consider dropping average assets as a proxy for start-up costs and entry barriers as one of the primary factors in size standards analysis.

Another commenter argued that while using average assets may be a useful method for assessing barriers to entry into the commercial market, it fails to capture the extensive administrative and compliance requirements associated with Federal contracts, the different skills required for Federal contracts as compared to the commercial market, and the size of contracts, all of which also act as significant entry barriers to the Federal market. The commenter recommended that SBA also evaluate the unique costs of entering the Federal marketplace.

SBA's response: Given the lack of actual data on various measures of start-up costs and entry barriers, including product differentiation, economies of scale, etc., SBA believes that average assets size does serve as a reasonable proxy for start-up costs and entry barriers. Industries with high average assets are likely to have higher capital requirements and greater barriers for new firms to enter the market, thereby supporting higher size standards, all else being equal. The evaluation of more, not fewer, factors will result in more robust and analytically sound size standards.

SBA agrees that these are several important factors determining businesses' ability to enter the Federal market and they should be considered when evaluating size standards. However, there exists no readily available data in a form to be able to formalize these factors in the size standards methodology. Given the lack of data, SBA believes that evaluation of small business Federal market share relative to small business share of the industry total revenues would provide a fairly good indication of how successful small businesses are in participating in the Federal market. In the Revised Methodology, SBA has expanded the analysis of Federal market conditions by including the odds that small businesses win a Federal contract in an industry. In addition, SBA also looks at the distribution of Federal contracts by firm size and size of contracts, when appropriate.

3. Industry competition: One commenter noted that evidence does not support using a 40 percent cut off of the four-firm concentration ratio (CR4) as a dividing line between competitive industries and oligopolistic industries or ones that are characterized by market dominance from a few firms. The commenter suggested that SBA should consider all CR4 values, not just those above the 40 percent threshold, as a measure of industry competition in establishing size standards. It would be methodologically more sound to use the CR4 statistic directly in the size standard interpolations to avoid double counting the receipts of the four largest firms, the commenter added.

Another, an industry association representing engineering firms, recommended that SBA consider using the "8-firm concentration ratio," which it claimed is also a widely accepted tool for measuring market share (although no references were provided



to support this claim) for evaluating industry competition. The commenter stated that the 8-firm concentration ratio provides a more accurate picture of market share controlled by the largest firms in an industry. According to the association, using the 8-firm concentration ratio, SBA may find that the largest firms control more than 40 percent in more industries than using the 4-firm concentration ratio and SBA may have to increase size standards for those industries.

SBA's response: SBA is aware of various measures (e.g., 4-firm ratio, 8-firm ratio, Herfindahl-Hirschman index, etc.) that are used to measure industry competition and dominance. Because the 4-firm ratio is simple for the public to understand and has long been used and accepted as an industry factor in size standards analysis, SBA continued using it until the recently completed comprehensive size standards review. This is also the most widely used measure in the relevant literature, as described in its Methodology. For these reasons, in the past SBA used the 40 percent 4-firm ratio as the dividing line between the competitive industries and concentrated industries. Further, the special tabulation of the 2002 Economic Census that SBA used for developing the Methodology and the 2007 Economic Census tabulation SBA used in the recently completed comprehensive size standards review only included data to compute the 4-firm concentration ratio, not the 8-firm ratio. However, using the 2012 Economic Census Tabulation, SBA has evaluated the appropriateness of using the 8-firm concentration ratio in the Revised Methodology to be used in the forthcoming review of size standards.

In response to the comment as well as based on its own evaluation of the current methodology, in the Revised Methodology, SBA is proposing to use all values of the 4-firm concentration ratios directly in the analysis, as opposed to using only 40 percent and

above. Accordingly, as explained in the Revised Methodology, the industries with lower 4-firm ratios will be assigned lower size standards and those with higher 4-firm ratios higher size standards, all else remaining the same. SBA also repeated the same analysis using the 8-firm concentration ratio. Because the results based on the 4-firm ratio were found to be quite comparable to the results based on the 8-firm ratio, SBA has decided to continue using the 4-firm ratio as the measure of industry competition.

4. Federal contracting factor: While commenters generally supported SBA's approach to assigning higher size standards for industries where small businesses are underrepresented in the Federal market relative to their share in the industry's total receipts, they offered suggestions for improvement. For example, one commenter expressed concern with reconciling SBA's approach to assigning a size standard based on Federal contracting factor and imposing a cap for the maximum size standard when the current size standard is at or near the maximum level. If SBA established a fixed increment in size standards levels with no maximum cap, it would provide the flexibility to increase size standards, when necessary, based on the Federal contracting factor, the commenter noted. Another commenter stressed the need to consider barriers to enter to Federal market as a factor in size standards analysis. A few commenters to the proposed rules for various NAICS sectors recommended giving the Federal contracting factor a greater weight to reflect administrative and compliance requirements and different skills required for Federal contracts, and size of contracts.

One commenter recommended that SBA should assess the extent to which contracts are being set aside within specific industries. The commenter argued that a higher size standard may not necessarily lead to a higher small business share in Federal

market in an industry if small business set-asides are not used in that particular industry.

SBA's goal should be to spread all small business contracting opportunities across all industries, because raising size standards may not have any impact if Federal agencies are over-relying on set-aside contracts only in a handful of industries to meet their small business contracting goals.

One commenter on construction size standards suggested that SBA should consider median size of Federal contracts when establishing size standards. The current method does not consider the Federal contracting trends in particular markets, the commenter noted. Either the bundling or contract consolidation should be curtailed or size standards increased, the commenter added.

SBA's response: In the Revised Methodology, SBA is not applying a fixed number of size standards levels or "bands" and is letting the data determine an appropriate size standard for each NAICS industry, with appropriate rounding as explained elsewhere in this notice and the Revised Methodology. However, SBA will continue its policy of capping the maximum size standard at a certain level. As noted earlier, allowing the data to determine a size standard without a cap would result in very high size standards for some industries, enabling very large businesses, possibly with billions in revenue or tens of thousands of employees, to qualify as small at the expense of genuine small businesses that need Federal help the most. However, in the Revised Methodology, SBA is including a much more comprehensive measure of small business participation and success in the Federal market.

Federal procurement is one of the factors SBA evaluates, along with industry data and other relevant considerations, when reviewing a size standard. The SBA's

Methodology permits, if necessary, a higher weight to the Federal contracting factor. However, SBA is concerned that giving an excessive weight to Federal procurement may produce skewed results with unintended adverse impact on small businesses. For procurement sensitive industries, SBA might consider giving a greater weight to the Federal contracting factor, and possibly evaluating additional data related to Federal contracts, where appropriate. For the recently completed comprehensive size standards review, SBA considered the Federal procurement factor for those industries that received \$100 million or more in total Federal contracts annually and showed a large disparity between small business shares in the Federal market and the industry's total sales.

While SBA agrees that small business opportunities should spread across all industries, it does not believe that size standards are the only factor driving Federal agencies' small business set-aside decisions in the various industries. SBA's size standards establish eligibility for the small business set-aside opportunities that Federal agencies provide in a particular industry, but they do not dictate how the agencies make their set-aside decisions. The number of set-asides in each industry can be a function of many factors, including the nature, scope, types, volume, and costs of goods and services the agencies need to procure. It should also be noted that the current 23 percent small business contracting goal only applies to total procurements government-wide, not to individual industries.

As mentioned earlier, there is a lack of data on administrative and compliance requirements and different skills required to participate in government contracting for SBA to be able to formalize these factors and assign a specific weight for the Federal contracting factor for specific industries. Implicitly, in the recently completed

comprehensive size standards review, SBA gave more weight to the Federal contracting factor in some industries than in others by assigning higher size standards for those industries that had \$100 million or more in annual Federal contracting and a lower small business share in the Federal market relative to their share in industry's total sales. In the Revised Methodology, SBA is reducing that threshold to \$20 million and including the estimated odds that small businesses will win a Federal contract in each industry, as an additional Federal contracting factor.

SBA does not agree that it does not consider Federal contracting trends when establishing size standards. SBA compares the small business share of Federal contracts with the small business share of total receipts for each industry. Specifically, if the small business share of contract dollars is substantially lower than the small business share of total receipts, SBA proposes a size standard that is higher than the current standard.

### **Comments on Measures of Business Size**

One commenter to the SBA's Methodology recommended that SBA use the measure of firm size that best represents the magnitude of a business operation within an industry and that indicates the level of the business activity generated by firms.

Accordingly, the commenter argued that subcontracting should support the number of employees as a measure of business size for size standards, not average annual receipts as SBA proposed. The commenter contended that when there is subcontracting, receipts leads to double counting and does not provide a good measure of the level of real economic activity. SBA's justification of using receipts when there is subcontracting conflicts with its justification to use employees when there exists variation in the degree of vertical integration, the commenter added.

Several commenters to the proposed rule for NAICS Sector 54 (76 FR 14323 (March 16, 2011)) argued that number of employees is a better measure of business size, especially for architectural and engineering industries where “pass throughs” are high and receipts are much more sensitive to business cycles, costs of materials, and inflation in the economy. One commenter to the Sector 48-49 proposed rule (76 FR 27935 (May 13, 2011)) suggested that SBA take into account the costs of materials and labor and establish size standards in terms of gross profits, instead of total receipts. One commenter to the Sector 23 proposed rule (77 FR 42197 (July 18, 2012)) argued that small business size standards for construction industries should be based on number of full time equivalent (FTE) employees, rather than on average annual receipts. Receipts are a “misleading indicator” for size of construction companies due to sharp increases in material costs, the commenter noted. In addition, the commenter maintained that a construction company’s gross receipts are inflated relative to the size standard as subcontracting and material costs that could account for as much as 85 percent of work being performed.

One commenter to the Sector 31-33 proposed rule (79 FR 53647 (September 10, 2014)) suggested to include, in addition to employee counts, other criteria for establishing size standards for manufacturing industries, such as business tenure (5 years), subcontracting limitations, revenue limits (\$30 million), and net worth limits (\$5 million).

#### SBA’s Response

First, Congress directs SBA to establish size standards for manufacturing concerns using number of employees and service concerns using average annual receipts. 15 USC 632(a)(2)(C). Further, for industries where subcontracting or “pass throughs”

are common, an employee based size standard may encourage businesses to excessively outsource Federal work to other businesses in order to remain within the size standard. Under the receipts based standard, businesses are not allowed to deduct the value of any work outsourced.

SBA also does not accept the suggestion to establish size standards in terms of gross profits. For a vast majority of industries, SBA uses either average annual receipts or number of employees as a measure of business size for size standards purposes. If a size standard were established in terms of gross profits, a company with hundreds of millions of revenues and thousands of employees can qualify as small under a profits-based size standard. It is not unusual for very large companies to have little or negative profit over the course of business cycles. Such a firm would clearly be “dominant” in the industry and thus not a small business under the statutory requirement that a small business is one that is independently owned and operated and not dominant in its field of operation. Moreover, a firm’s profits can be manipulated and thus would be an inconsistent and misleading measure of firm’s size for size standards purposes.

SBA disagrees that receipts based standards do not properly reflect the size of companies in the construction industry. Receipts, as a representative of the overall value of a company’s entire portfolio of work completed in a given period of time, are a better measure of the size of a construction company to determine its eligibility for Federal assistance. Annual receipts measure the total value of a company’s completed work. Under SBA’s prime contractor performance requirements (see 13 CFR 125.6, limitations on subcontracting), a general construction company needs to perform as little as 15 percent of the value of work and a specialty trade contractor can perform as little as

25 percent of the work with their own resources. SBA is concerned that employee based size standards could encourage construction companies near the size standard to subcontract more work to others to bypass the limitations on subcontracting and remain technically a small business. Regardless of the amount of work a company subcontracts to others, it is still part of its annual revenue, because the company is responsible for the entire contract. In other words, under a receipts based size standard, the company cannot deduct subcontracting costs from the average annual receipts calculation. Under the employee based size standard, companies would not count their subcontractors' employees to calculate their total number of employees. A company that subcontracts a lot of its work to others will have a considerably fewer employees than one that performs most of its work in-house.

Regarding the comment that receipts are not an appropriate measure of size for construction businesses because they are too sensitive to increases in material costs and fluctuations in market conditions, SBA adjusts all monetary based size standards at least every five years and more frequently if necessary. Similarly, to minimize the impacts of fluctuations in market conditions, SBA calculates the receipts for size standards purposes as the average annual receipts over the preceding three completed fiscal years.

In 2004, SBA proposed to replace average annual receipts with number of employees as the measure of size standards for most industries, including construction (see 69 FR 11129 (March 19, 2004)). Commenters in the construction industry generally opposed SBA's proposal for a number of reasons, such as those SBA states above. In addition, because employee based size standards are based on the average number of employees per pay period for the preceding 12 calendar months, businesses would have



to recalculate their size every month. Receipts, on the other hand, are calculated as the annual average over last three fiscal years and need to be updated only annually. This allows for fluctuations in market conditions. Employment data from the U.S. Census Bureau (Economic Census and County Business Patterns) and from other Federal statistical agencies (such as Bureaus of Economic Analysis and Labor Statistics) that SBA uses in its size standards analysis are based on total head counts of part-time, temporary and full-time employees, not based on FTEs. In other words, part-time employees are counted the same as full-time employees. In addition, using FTEs as a measure of size may increase reporting and record keeping requirements for small businesses to qualify for Federal programs. Thus, SBA is not adopting FTEs as a measure of size standards.

Incorporation of net worth into SBA's table of size standards is not practicable. It is not a value that lends itself to comparing businesses in a particular industry. A company's net worth can be affected by a number of things, such as debt, repurchased corporate stock, etc. Furthermore, data on net worth is not available by industry. Other criteria proposed by the commenter would, SBA believes, be too nebulous, temporary, and subjective and therefore not useful when establishing size standards that usually must remain static and in place for a number of years. Establishing small business eligibility based on the combination of multiple criteria (such as revenue limit, net worth limit, and employee count), as suggested by the commenter, would create unnecessary complexity to and confusion with size standards.

### **Comments on Data Sources and Issues**

SBA received a number of comments on various data sources it uses to evaluate industry and Federal procurement factors in developing or reviewing size standards, in particular the Economic Census and Federal Procurement Data System – Next Generation (FPDS-NG). Specifically, commenters contended that the Economic Census data that SBA uses in size standards analysis did not adequately reflect the conditions in their industries and recommended using alternative data sources. However, with a few exceptions, commenters did not provide alternative data or sources. When alternative data or their sources were provided, such data was either not complete or not representative of the overall industry. A few commenters pointed out that the Economic Census data were outdated and did not reflect current industry structure. Some commented that the Economic Census includes revenues from non-Federal work, international work, and work in non-primary industry in revenues for primary industry, thereby distorting average firm size and estimated size standards.

One commenter stated that the FPDS-NG data does not provide a complete picture of small business participation in the Federal marketplace. Specifically, the commenter pointed out that there exist no data on work that large prime contractors subcontracted to small businesses, on work subcontracted to large firms by small prime contractors, and on the size of firms performing Federal work within small and large business categories. Citing these problems, the commenter stated that there is no way of knowing exactly how successful and competitive small businesses are in the Federal market under the current size standards. Additionally, the commenter contended that due to the lack information on the exact sizes of businesses receiving Federal contracts, it is

difficult to estimate the impact of size standards changes on small business participation in Federal market.

#### SBA's Response

The Economic Census is the most comprehensive data source available to evaluate industry characteristics. The Economic Census data provides a complete and actual representation of an industry structure, because, by law, all firms are required to respond to the Economic Census. For these reasons, SBA will continue to use the Economic Census as the principal source of industry data for its size standards analyses and reviews. However, the Agency will give due considerations to alternative data provided by the industry participants, especially if such data is representative of the entire industry in question.

The Economic Census tabulations that SBA receives from the U.S. Census Bureau are based on primary industry at the establishment level. Establishments doing some work in an industry may not be included in that industry if that is not their primary work. SBA is aware of this and other problems with the Economic Census data. For industries where such problems are significant, SBA also evaluates the System for Award Management (SAM) and FPDS-NG data to evaluate industry characteristics. While SBA is attentive to a substantial lag that exists between the times when Economic Census data is collected and when the data becomes available, the Economic Census is still the latest and most comprehensive data source available out there for evaluating all industries in a consistent manner.

SBA does not agree that industry's revenues reported in the Economic Census are distorted for size standards analysis because they include non-federal, non-primary and

overseas activities. First, revenues that U.S. companies generate in foreign countries are not, by design, included in the Economic Census. Second, including revenues from non-federal or non-primary activities in an industry's revenues is consistent with how SBA calculates revenues for size standards purposes. In other words, when calculating a company's total revenues for size standards purposes, revenues that the company has received from all sources (including Federal, state, and private work, and work related to non-primary industries) must be counted. See 13 CFR 121.104.

SBA is aware that the FPDS-NG data does not contain information on subcontracting. The Electronic Subcontracting Reporting System (eSRS) collects data on subcontracting activity, but those data are not available by NAICS industry. However, despite these and other issues as discussed in the Revised Methodology, SBA believes that FPDS-NG is still the best data source available for assessing the small business participation in the Federal marketplace. Prior to 2013 when FPDS-NG data did not include exact size of the companies receiving contracts, SBA obtained size of contract recipients by merging the FPDS-NG data with employees and revenues information from SAM, formerly Central Contractor Registration (CCR). By using this analysis in conjunction with the share of small businesses in the Federal market relative to their share in overall industry total sales, SBA assessed the impacts of proposed size standards changes on small business participation in the Federal market. Now, SBA estimates the impacts of size standards changes by using small business goaling data, which includes the actual size of contract recipients.

### **Comments on Small Business Size Definitions and Related Issues**

A number of commenters to the proposed rules for various NAICS sectors asserted that SBA's small business size standards did not represent "truly small" businesses. Many stated that SBA's size standards included up to 99 percent of all businesses as small. One commenter added that SBA's small business definitions are much larger than those used by other countries (such as Australia and European Union) and by the U.S Congress, for example, for the Affordable Health Care Act.

#### **SBA's Response**

SBA acknowledges that in some industries its size standards could include up to 97-99 percent of all firms as small. However, while that might appear to be a large segment of an industry in terms of the percentage of firms, for a majority of industries small businesses only account for less than 50 percent of total industry receipts and less than 25 percent of total Federal contract dollars. It is not uncommon for a small number of large firms to have a high percentage of industry receipts and employees and to obtain the bulk of Federal contacts. These are important considerations when establishing or reviewing small business size standards. Additionally, while SBA's size standards include more than 90 percent of firms for most industries, the Agency ensures that no business concern that qualifies as "small" is dominant in its industry.

Common dictionary definitions of what is "small" are not relevant to why and how SBA establishes small business size standards. SBA's definition of a small business concern is more than a general meaning of the word "small" in a dictionary. In addition, numeric small business size standards are just one component of what constitutes a small business concern under SBA's regulations. SBA's size standards set thresholds on how

large a business concern can be and still qualify as small for various Federal government programs. If a firm (together with its affiliates) meets both SBA's definition of a business concern (see 13 CFR 121.105) and its numeric size thresholds (§121.201), it is a small business concern; if it does not meet both SBA's definition of a business concern and its numeric size thresholds, it is considered "other than small." The "dictionary" definitions of "small" usually speak in very general terms. However, under SBA's size standards, a company that qualifies as "small" in one industry may not qualify as "small" in another industry, because being small is relative to other business concerns in the same field of operation.

What constitutes a small business in other countries does not apply and has no relevance to SBA's small business definitions and U.S. Government programs that use them. Likewise, SBA's small business size standards are not relevant to programs of other countries. Depending on their economic and political realities, other countries have their own programs and priorities that can be very different from those in the U.S. Accordingly, small business definitions other countries use for their government programs can be vastly different from those established by SBA for U.S. Government programs. From time to time, the U.S. Congress has used different thresholds, sometimes below the SBA's thresholds, to define small firms under certain laws or programs, but those thresholds apply only to those laws and programs and generally are of no relevance to SBA's size standards. SBA establishes size standards, in accordance with the Small Business Act, for purposes of establishing eligibility for Federal small business procurement and financial assistance programs. The primary statutory definition of a small business is that the firm is not dominant in its field of operation. Accordingly,

rather than representing the smallest size within an industry, SBA's size standards generally designate the largest size that a business concern can be relative to other businesses in the industry and still qualify as small for Federal government programs that provide benefits to small businesses.

### **Comments on Mid-Sized Business Concerns**

Several comments to the proposed rule for NAICS Sector 54 recommended a number of alternatives to enable currently large but formerly small firms (which they called as "mid-sized" businesses) to obtain Federal contracts. Those alternatives and SBA's responses are discussed below.

Define as small businesses all those which are not dominant in their field of operation, in accordance with the Section 3(a)(1) of the Small Business Act. For example, consider the average size of the largest or dominant businesses in an industry and determine the size standard as a percentage of that average.

SBA's response: SBA does not adopt this recommendation. As described in its Methodology and all proposed rules, in establishing or modifying size standards, SBA considers various industry factors (e.g., average size, industry concentration, and distribution of firms by size) to identify the small business segment of an industry. The Small Business Act provides that a business concern defined as small cannot be dominant in its field of operation. SBA has implemented this provision of the Act by ensuring that a size standard based on its industry analysis does not include a business concern that is dominant in its industry. For this, SBA generally evaluates the market share of a firm that qualifies as small under a proposed or revised size standard and distribution of firms by size. If the results show the largest or potentially dominant firms qualifying as small

under the proposed or revised size standard, SBA lowers the size standard. The legislative history of the Act does not imply that a firm that is not dominant in its field can automatically be defined as small. Size standards based on the average size of the largest or dominant businesses in an industry could result in a size standard that will enable extremely large businesses to qualify as small, thereby hurting truly small businesses that need the Federal assistance the most.

Develop multi-tiered employee size standards based on the size of a Federal contract, such as a size standard of 50 employees for contracts valued at less than \$5 million, of 51-150 employees for contracts valued at \$5 million to \$50 million, ..., , and of 1,001-2,000 employees for contracts valued at \$500 million or more.

SBA's response: While this approach may offer Federal contracting opportunities for various small and mid-sized businesses, SBA does not adopt this recommendation for several reasons. First, SBA believes that such tiered size standards within each industry would add significant complexity to size standards, which many believe are already too complex. Second, in order for the tiered size standards approach to work, Congress would need to establish new small business procurement goals for each tier to ensure that small businesses at different tiers have a fair access to Federal contracts. Third, this would warrant much more burdensome system and reporting and requirements (e.g., SAM and FPDS-NG) than those that currently exist and the small business Federal procurement programs would become significantly more complex to administer. Fourth, the Small Business Act authorizes SBA to establish one definition of what is a small business concern, not tiered definitions of what is "small," "medium," and so forth. Fifth, past programs that applied the tiered small business approaches, such as the Very



Small Business Program and the Emerging Small Business category under the CompDemo Program, were not successful and were eventually repealed by Congress.

Establish separate size standards for Federal contracting. Commenters stated that Federal contracting imposes restrictions on business practices and operations not included in the commercial market. They argued that given the differences between commercial and government work, a separate set of size standards are warranted for Federal procurement.

SBA's response: SBA does not adopt this recommendation. Federal procurement is already one of the primary factors SBA considers when developing or reviewing size standards. However, giving an excessive weight to Federal procurement may produce size standards that are likely to be biased in favor of more successful Federal contractors, which in turn would reduce contracting opportunities for smaller and emerging businesses. For procurement sensitive industries, however, SBA may consider giving a greater weight to the Federal contracting factor and possibly evaluating additional data related to Federal contracts. Additionally, in a number of industries, SBA has established separate size standards for Federal contracts of very specific types of goods and services, which are usually known as "exceptions" in the SBA's table of size standards.

SBA is also concerned that if separate size standards for Federal procurement are appreciably higher than the current size standards, that may cause significant disadvantage to very small businesses when they compete for Federal small business set-aside contracts.

Calculate average annual receipts based on five years. The commenter also recommended calculating average annual receipts over the preceding five years,

instead of three. The commenter alleged that this would allow small businesses to plan and increase capacity before entering full and open competition and provide longer transition time from small business status to other than small business status. In addition, small businesses with large temporary increases in revenues for one or two years would not lose their small business status.

SBA's response: SBA does not adopt this comment. SBA believes that calculating average annual receipts over three years ameliorates fluctuations in receipts due to variations in economic conditions. SBA maintains that three years should reasonably balance the problems of fluctuating receipts with the overall capabilities of firms that are about to exceed the size standard. Extending the averaging period to five years would allow a business to greatly exceed the size standard for some years and still be eligible for Federal assistance, perhaps at the expense of other smaller businesses. Such a change is more likely to benefit successful small business graduates by allowing them to prolong their small business status, thereby reducing opportunities for currently defined small businesses.

#### **Comments on Tiered Size Standards**

Several comments to the Sector 54 proposed rule recommended that SBA establish some form of tiered size standards for Federal contracting, including a “micro-business” category to help truly small businesses that are way below the current size standards. Similarly, one commenter on the Sector 48-49 proposed rule stated that more than two-thirds of companies registered in SAM have fewer than 20 employees and argued that those are the companies that need Federal support the most. The commenter suggested that, for goods producing industries, businesses with fewer than 20 employees

should be classified as “small business” and contracts valued at \$150,000 or less should be set-aside only for those businesses. Similarly, according to the commenter, businesses with 20-40 employees should be classified as “medium sized small business” and contracts between \$150,000 and \$500,000 should be reserved for those businesses. For services industries, less than \$100,000 in sales should be labeled as “small business,” \$300,000 as “medium sized small business” and \$500,000 or more as “large small business,” the commenter suggested. A commenter to the proposed rule for Sector 44-45 also suggested that SBA designate a separate sub-group of truly small businesses and give them special preference when competing for smaller government contracts.

#### SBA’s Response

SBA does not adopt the commenters’ suggestions to establish “micro-business” or “tiered” size standards for several reasons. First, SBA is concerned that very small or “micro” size standards, such as those suggested by the commenters, may not adequately capture the small business segment in an industry that small business programs are intended to help. The size standards should be such that small businesses are able to grow and develop to an economically viable size while remaining eligible for Federal assistance. If size standards were set too low, small businesses will quickly outgrow the size standards and be forced to compete with significantly larger businesses for Federal contracts under full and open competition. However, as stated elsewhere in this notice, SBA is also equally concerned about setting size standards too high, as doing so could put smaller businesses at a disadvantage in competing for Federal opportunities. Second, such tiered size standards would add significant complexity to size standards, which many believe are already too complex. Third and most importantly, the Small Business

Act requires SBA to establish one definition of what is a small business concern, not what is “very small,” “small,” “medium-sized,” and so forth. Also, as stated elsewhere, for tiered size standards to work and benefit small businesses, Congress needs to enact small business contracting goals for various tiers to ensure that small businesses at each tier have a fair share of Federal contracts.

### **Comments on Fixed Number of Size Standards**

Commenters generally supported SBA’s Methodology and its proposal to use a fixed number of size levels to simplify size standards. There were a few who opposed fixed size levels and believed, because of wide gaps between the two successive size levels, calculated size standards could be larger or smaller than they should otherwise be.

One commenter contended that the Methodology does not provide a convincing economic basis for restricting size standards to a small number of fixed levels or “bands”. Similarly, it does not provide a reasoned, evidence-driven basis for instituting a 1,000-employee cap that is substantially below the 1,500-employee size standard currently used for 17 industries, the commenter added. The commenter argued that the imposition of the 1,000-employee cap for employee based size standards appears arbitrary. The Methodology would be more transparent and better reflect the economic characteristics of the industry if SBA let the data and analytical results determine the maximum size standard for an industry, the commenter suggested. The maximum size standard should be a conclusion of the SBA’s review and analysis of the data instead of being imposed as a constraint in the analysis and there is no reason to set an artificial cap on size standards, the commenter noted. Such a cap can only serve to restrict the SBA from providing support to small businesses that it intended to help.

### SBA's Response

The fixed size standard levels were developed to simplify size standards. There were 31 different levels of receipts based size standards at the start of the comprehensive size standards review, which SBA believed were both unnecessary and difficult to justify analytically with the available industry data. Thus, SBA adopted the fixed size standards approach and sought comments on whether more or fewer size standard levels are more appropriate.

In response to these comments and the amendment to the Small Business Act (section 3(a)(8)) under the National Defense Authorization Act of Fiscal Year 2013 (NDAA 2013) (P.L. 112-239, Section 1661, Jan. 2, 2013) requiring SBA to not limit the number of size standards, SBA has relaxed the limitation on the number of small business size standards in the Revised Methodology. Specifically, SBA is proposing to assign a separate size standard to each NAICS industry, with a calculated receipts based size standard rounded to the nearest \$500,000 and a calculated employee based size standard rounded to the nearest 50 employees for Manufacturing and industries in other sectors (except Wholesale and Retail Trade) and to the nearest 25 employees for Wholesale and Retail Trade. However, SBA has established the minimum and maximum size standard levels as its policy decisions such that businesses that qualify as small have adequate capabilities and resources to be able to perform government contracts and do not outcompete smaller businesses in accessing Federal assistance. Letting the data and analytical formulae alone determine the maximum size standard, as the commenter recommended, would result in a size standard for some industries that would enable quite large businesses, possibly with billions of revenues and thousands of employees, to

qualify as small at the expense of smaller businesses that need Federal assistance the most.

To be consistent with SBA's policy of not lowering any size standards in the recent comprehensive size standards, SBA retained the 500-employee minimum and 1,500-employee maximum size standards for all industries in the Manufacturing Sector and for most industries with employee based size standards not in Sectors 31-33, 42, and 44-45, although in the Methodology SBA had proposed setting the minimum size standard for those industries at 250 employees and the maximum size standard at 1,000 employees. Further, lowering a manufacturing size standard below 500 employees would conflict with the 500-employee size standard for non-manufacturers under the SBA's non-manufacturer's rule.

### **Comments on Anchor Size Standards**

Some commenters to the Sector 54 proposed rule questioned the rationale for using \$7 million as an anchor for receipts based standards. Similarly, a few commenters to the proposed rules for employee based size standards questioned 500 employees as an anchor for employees based size standards. One commenter to the proposed rule on employee based size standards for industries not part of Sectors 31-33, 42 and 44-45 argued that SBA's use of "anchor size standard" approach as a basis for evaluating characteristics of individual industries violated the statutory requirement on using common size standards.

### **SBA's Response**

SBA provided a detailed justification for using the "anchor size standard" approach in its Methodology". In fact, SBA has been using the "anchor" approach since

the 1980s when reviewing and modifying size standards without much concern from the public. The use of the “anchor” served an important function by ensuring that the characteristics of all industries are consistently evaluated relative to the same baseline level. Additionally, when the Methodology was prepared, the \$7 million anchor was the size standard for a majority of the industries that have receipts based size standards and 500-employee anchor applied to most industries that have employee based size standards. However, in response to the above comments and its own evaluation of the Methodology, in the Revised Methodology SBA is replacing the “anchor size standard” approach with a “quintile” approach to evaluating characteristics individual industries, as explained elsewhere in this document.

### **Comments on Levels of Size Standards**

A few questioned SBA’s Methodology on the ground that calculated size standards are generally much higher than average firm size for the industry. Some expressed concerns regarding the use of simple average firm size, instead of median firm size, and averaging of size standards over different factors. One commenter stated that SBA’s Methodology of averaging size standards supported by different factors to calculate an overall size standard may result in loss of information and contended that the averaging procedure hurts companies in the \$25.5 million to \$35.5 million annual revenue range. The commenter believed that perhaps assigning different weights to different factors would provide better results, but did not offer any specific suggestions on those weights.

### SBA's Response

The purpose of evaluating various industry characteristics is to describe quantitatively the structure of an industry. Since no single characteristic or factor can adequately describe industry structure, SBA evaluates several factors (such as average firm size, industry concentration, and distribution of market shares by size) to best obtain a full representation of industry structure. In addition, in most cases, equating the size standard to the average or median firm size can result in an unacceptably low size standard that may not adequately capture the small business segment of that industry that small business programs are intended to assist. Thus, for most industries, size standards are generally higher than the simple average or median firm size so that small businesses have room to grow and develop to an economically viable size while still remaining eligible for Federal assistance. If size standards were too low, small businesses would quickly outgrow the size standards and be forced to compete with significantly larger businesses for Federal contracts on a full and open basis. SBA is also equally concerned about setting size standards too high, as doing so could put smaller businesses at a disadvantage in competing for Federal opportunities.

SBA disagrees that calculating an industry's overall size standard as the average of size standards supported by each factor results in loss of information. In fact, this procedure preserves information provided by different factors, as opposed to basing the size standard only on one or two factors. Moreover, if the size standard was based on the largest value supported by any of the factors, it would put smaller companies at a competitive disadvantage. If warranted, SBA's Methodology allows assigning different weights to different factors.



### **Other Comments**

One commenter agreed with the Agency's position that lowering size standards under current economic conditions is not in the best interests of small business, but felt that increasing size standards by 180-300 percent at one time was also not in the best interests of small business. He stated that size standards should be raised between 50-75 percent and recommended a complete review of SBA's loan data, small business participation in Federal contracting, and other relevant factors within 2-3 years to determine if another increase is appropriate.

One commenter to the proposed rule on Sector 44-45 (74 FR 653924 (October 21, 2009)) suggested that there should be only one revenue based and only one employee based size standard, regardless of NAICS industry. Another commenter on the proposed rule on Sector 21 (77 FR 72766 (December 6, 2012)) suggested that all size standards should be capped at \$7 million in average annual receipts.

Two commenters on the Sector 31-33 proposed rule supported SBA's proposed five employee based size standard levels for Manufacturing and successive differences of 250 employees rather than 500 employees. However, one suggested that SBA should establish an additional level of 250 employees as the minimum size standard and set the maximum employee based standard at 1,000 employees. A lower size standard would protect emerging manufacturers that are not able to compete with established larger businesses, the commenter maintained. Both commenters argued that the Agency should lower size standards when the analysis supports lowering them. One argued that not lowering size standards would encourage manufacturers not to upgrade their facilities with advanced manufacturing techniques and allow larger manufacturers to compete with

true small manufacturers. While one commenter suggested that SBA should not adjust employee based size standards for labor productivity growth and focus on protecting emerging businesses instead, the other pointed out that the lack of data on labor productivity would make adjusting size standards based on labor productivity difficult. One commenter supported weighing all factors equally, while the other suggested weighing some factors more than others for certain industries.

Some commenters believed that SBA's Methodology was too complicated and difficult to understand.

#### SBA's Response

SBA agrees that the proposed increases to size standards were quite significant for some industries and the Agency had sought comments if the increases to size standards should be limited to certain amounts. Comments generally supported the Methodology, industry and program data it evaluated and its proposed increases to size standards. SBA believes that the changes in industry structure since the last comprehensive review of size standards nearly 30 years ago may have resulted in large increases to size standards for some industries. The Small Business Jobs Act of 2010 requires SBA to review all size standards at least once every five years and make adjustments to reflect market conditions. Prior to the next review, SBA will assess the impact of size standards revisions adopted in the current review.

Using only one receipts based standard and only one employee standard would conflict with the statutory requirement that "the [SBA] Administrator shall ensure that the size standard varies from industry to industry to the extent necessary to reflect the differing characteristics of the various industries and consider other factors deemed to be

relevant by the Administrator.” (15 U.S.C. 632(a)(3)). The relevant data show significant differences among industries and SBA believes that varying the size standard by industry not only complies with the Act, but it also serves the best interests of small businesses in that Sector.

Some of the issues the commenters raised regarding the minimum and maximum employee based size standards are addressed in the Revised Methodology. For example, SBA will continue to cap the maximum employee size standards for Manufacturing and industries in other sectors (except Wholesale and Retail Trade) at 1,500 employees, but will set the minimum employee size standard at 250 employees instead of 500. Additionally, the difference between the two successive employee size standards for those industries will be reduced to 50 employees. Employee size standards for Wholesale and Retail Trade will vary from 50 employees to 250 employees with an interval of 25 employees. With respect to SBA’s policy of not lowering size standards in the recent comprehensive size standards review, SBA provided a detailed explanation in each proposed rule with respect to why lowering size standards was not in the best interest of small businesses. SBA was concerned that lowering size standards (including the minimum and maximum levels) would have caused numerous small businesses to lose their eligibility for Federal programs and run counter to various legislative and Administration’s measures to help small businesses and the economy in the aftermath of the 2008-2009 great recession.

SBA’s Methodology provides a vast array of information on its size standards analysis from a general description of the analytical approach to rigorous mathematical expressions of the calculation of industry factors. While some portions of the document

are of somewhat technical nature, the public should be able to understand the general description of the various factors and data sources SBA uses when reviewing size standards.

### **Changes in the Revised Methodology**

The Revised Methodology, available on the SBA's website at [www.sba.gov/size](http://www.sba.gov/size), describes in details how SBA establishes, evaluates and adjusts its small business size standards pursuant to the Small Business Act (Act) and related legislative guidelines. Specifically, the document provides a brief review of the legal authority and early legislative and regulatory history of small business size standards, followed by a detailed description of the size standards analysis.

Section 3(a) of the Small Business Act; 15 U.S.C. § 632(a) (Public Law 85-536, 67 Stat. 232, as amended), provides the SBA's Administrator (Administrator) with authority to establish small business size standards for Federal government programs. The Administrator has discretion to determine precisely how the Administrator should establish small business size standards. The Act and its legislative history highlight three important considerations for establishing size standards. First, size standards should vary from industry to industry according to differences among industries. 15 U.S.C. § 632(a)(3). Second, a firm that qualifies as small shall not be dominant in its field of operation. 15 U.S.C. §632(a)(1). Third, pursuant to 15 U.S.C. §631(a), the policies of the Agency should assist small businesses as a means of encouraging and strengthening their competitiveness in the economy. These three considerations continue to form the basis for the SBA's methodology for establishing, reviewing, or revising small business size standards.

### Industry Analysis

SBA examines the structural characteristics of an industry as a basis to assess industry differences and the overall degree of competitiveness of an industry and of firms within the industry. As described more fully in the Revised Methodology document, SBA generally evaluates industry structure by analyzing four primary factors – average firm size (both simple and weighted average), degree of competition within an industry (4-firm concentration ratio), start-up costs and entry barriers (average assets as a proxy), and distribution of firms by size (Gini coefficient). This approach to assessing industry characteristics that SBA has applied historically remains very much intact in the Revised Methodology. As the fifth primary factor, SBA assesses the ability of small businesses to compete for Federal contracting opportunities under the current size standards. For this, SBA examines the small business share of total Federal contract dollars relative to the small business share of total industry's receipts for each industry. To better assess the small business participation in Federal contracting, in the Revised Methodology, SBA also includes the odds that small businesses will win Federal contracts as an additional component of the Federal contracting factor. SBA also considers other secondary factors as they relate to specific industries and interests of small businesses, including technological change, competition among industries, industry growth trends, and impacts of the size standards on SBA programs.

While the factors SBA uses to examine industry structure remain intact, its approach to assessing the differences among industries and translating the results to specific size standards has changed in the Revised Methodology. Specifically, in response to the public comments against the “anchor” size standards approach applied in

the latest review of size standards (discussed above), recent amendment to the Act limiting the use of common size standards (see section 3(a)(7)) of the Act) under the National Defense Authorization Act of Fiscal Year 2013 (NDAA 2013) (Public Law 112-239, Section 1661, Jan. 2, 2013), and SBA’s own review of the Methodology, in the Revised Methodology, SBA replaces the “anchor” approach with a “percentile” approach as an analytical framework for assessing industry differences and deriving a size standard supported by each factor for each industry.

Under the “anchor” approach, SBA generally compared the characteristics of each industry with the average characteristics of a group of industries associated with the “anchor” size standard. For the recent review of size standards, the \$7 million was the “anchor” for receipts based size standards and 500 employees was the “anchor” for employee based size standards (except for Wholesale Trade and Retail Trade). If the characteristics of a specific industry under review were similar to the average characteristics of industries in the anchor group, SBA generally adopted the anchor as the appropriate size standard for that industry. If the specific industry’s characteristics were significantly higher or lower than those for the anchor group, SBA assigned a size standard that was higher or lower than the anchor. To determine a size standard above or below the anchor size standard, SBA evaluated the characteristics of a second comparison group. For industries with receipts based size standards, the second comparison group consisted of industries with size standards between \$23 million and \$35.5 million, with the weighted average size standard for the group equaling \$29 million. For manufacturing industries and other industries with employee based size standards (except for Wholesale Trade and Retail Trade), the second comparison group

included industries with a size standard of 1,000 employees or 1,500 employees, with the weighted average size standard of 1,323 employees. Using the anchor size standard and average size standard for the second comparison group, SBA computed a size standard for an industry's characteristic (factor) based on the industry's position for that factor relative to the average values of the same factor for industries in the anchor and second comparison groups.

In the past, including the recent review of size standards, the anchor size standards applied to a large number of industries, making them a good reference point for evaluating size standards for individual industries. For example, at the start of the recent review of size standards, the \$7 million (now \$7.5 million due to the adjustment for inflation in 2014) anchor standard was the size standard for more than 70 percent of industries that had receipts based size standards. Similarly, a similar proportion of industries with employee based size standards had the 500-employee anchor standard. However, when the characteristics of those industries were evaluated individually, for a large majority of them the results yielded a size standard different from the applicable anchor. Consequently, now just 24 percent industries with receipts based size standards and 22 percent of those with employee based size standards have the anchor size standards. Additionally, section 3(a)(7)) of the Act limits the SBA's ability to create common size standards by grouping industries below the 4-digit NAICS level. The "anchor" approach would entail grouping industries from different NAICS sectors, thereby making it inconsistent with the statute.

Under the "percentile" approach, in the Revised Methodology, SBA will rank each industry within a group of industries with the same measure of size standards using

each of the four industry factors. As stated earlier, these four industry factors are average firm size, average assets size as proxy for startup costs and entry barriers, industry competition (4-firm concentration ratio), and distribution of firms by size (Gini coefficient). As detailed in the Revised Methodology, the size standard for an industry for a specific factor will be derived based on where the factor of that industry falls relative to other industries sharing the same measure of size standards. If an industry ranks high for a specific factor relative to most other industries, all else remaining the same, a size standard assigned to that industry for that factor will be higher than those for most industries. Conversely, if an industry ranks low for a specific factor relative to most industries in the group, a lower size standard will be assigned to that industry. Specifically, for each industry factor, an industry is ranked and compared with the 20<sup>th</sup> percentile and 80<sup>th</sup> percentile values of that factor among the industries sharing the same measure of size standards (i.e., receipts or employees). Combining that result with the 20<sup>th</sup> and 80<sup>th</sup> percentile values of size standards among the industries with the same measure of size standards, SBA computes a size standard supported by each industry factor for each industry. The Revised Methodology provides detailed illustration of the statistical analyses involved in this approach.

#### Number of Size Standards

To simplify size standards, in the recent review, SBA applied a limited number of fixed size standards: eight revenue based size standards and eight employee based size standards. In response to comments against the fixed size standards approach (as discussed above) and section 3(a)(8) of the Act requiring SBA to not limit the number of size standards, in the Revised Methodology, SBA has relaxed the limitation on the



number of small business size standards. Specifically, SBA will calculate a separate size standard for each NAICS industry, with a calculated receipts-based size standard rounded to the nearest \$500,000 and a calculated employee-based size standard rounded to the nearest 50 employees for Manufacturing and industries in other sectors (except Wholesale and Retail Trade) and to the nearest 25 employees for Wholesale and Retail Trade.

However, as a policy decision, SBA will continue to maintain the minimum and maximum size standard levels. Accordingly, SBA will not generally propose or adopt a size standard that is either below the minimum or above the maximum level, even though the calculations might yield values below the minimum or above the maximum. The minimum size standard generally reflects the size a small business should be to have adequate capabilities and resources to be able to compete for and perform Federal contracts. On the other hand, the maximum size standard represents the level above which businesses, if qualified as small, would cause significant competitive disadvantage to smaller businesses when accessing Federal assistance. SBA's proposed minimum and maximum size standards are shown in Table 1, "Minimum and Maximum Receipts and Employee Based Size Standards," below.

**Table 1**  
Minimum and Maximum Receipts and Employee Based Size Standards

Type of size standards	Minimum	Maximum
Receipts-based size standards (excluding agricultural industries in Subsectors 111 and 112)	\$5 million	\$40 million
Receipts-based size standards for agricultural industries in Subsectors 111 and 112	\$1 million	\$5 million
Employee-based standards for Manufacturing and other industries (except Wholesale and Retail Trade)	250 employees	1,500 employees
Employee-based size standards in Wholesale and Retail Trade	50 employees	250 employees

With respect to receipts based size standards, SBA is proposing \$5 million and \$40 million, respectively, as the minimum and maximum size standard levels (except for most agricultural industries in Subsectors 111 and 112). These levels reflect the current minimum receipts-based size standard of \$5.5 million and the current maximum of \$38.5 million, rounded for simplicity. Section 1831 of NDAA 2017 amended the Act directing SBA to establish and review size standards for agricultural enterprises in the same manner it establishes and reviews size standards for all other industries. However, the evaluation of the industry data from the 2012 Census of Agriculture seems to suggest that \$5 million minimum and \$40 million maximum size standards would be too high for agricultural industries in Subsectors 111 and 112. Accordingly, SBA proposes \$1 million as the minimum size standard for industries in Subsector 111 (Crop Production) and Subsector 112 (Animal Production and Aquaculture). A vast majority of agricultural industries in those subsectors currently have a \$750,000 receipts-based size standard, which was established by Congress in 2000 (Public Law 106-554, 114 Stat. 2763, Dec. 21, 2000). Considering inflation since then, that is equivalent to a little over \$1 million today. Based on the evaluation of the industry data, SBA is proposing \$5 million as the maximum size standard for agricultural industries in those two subsectors. Regarding employee based size standards, SBA's proposed minimum and maximum levels for manufacturing and other industries (excluding Wholesale and Retail Trade) reflect the current minimum and maximum size standards among those industries. For employee based size standards for wholesale and retail trade industries, the proposed minimum and maximum values are the same as what SBA proposed in its 2009 Methodology.

### Evaluation of Federal Contracting Factor

In the Revised Methodology, SBA has expanded and modified its approach to incorporating the Federal contracting factor in the size standards analysis. In addition to evaluating small business participation in Federal contracting in terms of the share of total Federal contract dollars awarded to small businesses, in the Revised Methodology, SBA is also including the odds that small businesses win Federal contracts under the current size standard.

For each industry, SBA compares the small business share of total Federal contract dollars to the share of total industrywide receipts attributed to small businesses. In general, if the share of Federal contract dollars awarded to small businesses in an industry is significantly smaller than the small business share of total industry's receipts, *ceteris paribus*, a justification would exist for considering a size standard higher than the current size standard. In cases where small business share of the Federal market is already appreciably high relative to the small business share of the overall market, it would generally support the current size standards.

To determine how likely or unlikely small businesses are to win Federal contracts in each industry, as part of the Federal contracting factor, in the Revised Methodology, SBA estimates the odds that small businesses win Federal prime contracts under the existing size standards. If the estimated odds of winning Federal contracts by small businesses in an industry are found to be significantly lower than one, it would suggest that small businesses are not successful in winning the contracts in that industry and support raising the current size standard. If those odds are greater than or equal to one, it would indicate that small businesses are successful in receiving Federal contracts,

thereby supporting the current size standard. Small businesses may have the lower odds of receiving Federal contracts in an industry for several reasons, including, but not limited to: (i) the industry is associated with higher capital requirements and other barriers for small businesses to enter the Federal market and win contracts, (ii) small businesses under the industry's current size standard lack adequate technical capabilities, expertise and experience to be able to perform Federal contracts, and (iii) the industry does not have an adequate pool of qualified small businesses, forcing Federal agencies to offer contracts mostly on an unrestricted or full and open competition basis. All else being the same, all these reasons would provide support to increase the size standard. The analytical approach to estimating the odds of winning Federal contracts is detailed in the Revised Methodology.

In the methodology used in the recent review of size standards, SBA evaluated the Federal contracting factor only for those industries that averaged \$100 million or more in Federal contracts annually. The latest FPDS-NG data suggests that the \$100 million threshold is too high, rendering the Federal contracting factor irrelevant for more than 80 percent of industries. Accordingly, in the Revised Methodology, SBA evaluates the Federal contracting factor for industries (except those in Wholesale Trade and Retail Trade) averaging \$20 million or more in Federal contract dollars annually. Because NAICS codes in Wholesale Trade and Retail Trade do not apply to Federal procurement, SBA does not consider the Federal contracting factor for evaluating size standards industries in those sectors.

### Evaluation of Industry Competition

For the reasons provided in the Revised Methodology, SBA continues to use the 4-firm concentration ratio as a measure of industry competition. In the past, SBA did not consider the 4-firm concentration ratio as an important factor in size standards analysis when its value was below 40 percent. If an industry's 4-firm ratio was 40 percent or higher, SBA used the average size of the four largest firms as a primary factor in determining a size standard for that industry. In response to the comment as well as based on its own evaluation of industry factors, in the Revised Methodology, SBA is proposing to apply all values of the 4-firm concentration ratios directly in the analysis, as opposed to using the 40 percent rule. Based on the 2012 Economic Census data, the 40 percent rule applies only to about one-third of industries for which 4-firm ratios are available. For the same reason, SBA is also dropping the average firm size of the four largest firms. Moreover, the four-firm average size is found to be highly correlated with the weighted average firm size, which is used as a measure of average firm size.

### Summary of and Reasons for Changes

Table 2, "Summary of and Reasons for Changes," below, summarizes what has changed from the current methodology to the revised one and impetus for such changes, specifically whether the changes reflect the statutory requirements, public comments on the current methodology, or analytical improvements/refinements based on SBA's own review of the methodology.

Table 2  
Summary of and Reasons for Changes

Process/ Factor	Current	Revised	Reason
Industry analysis	“Anchor” approach. Average characteristics of industries with so called “anchor” size standards formed the basis for evaluating individual industries.	“Percentile” approach. The 20 <sup>th</sup> and 80 <sup>th</sup> percentile values for industry characteristics form the basis for evaluating individual industries.	<ul style="list-style-type: none"> <li>• Section 3(a)(7) of the Small Business Act limits use of common size standards only to the 4-digit NAICS level.</li> <li>• The percentage of industries with “anchor” size standards decreased from more than 70 percent at the start of the recent size standards review to less than 25 percent today.</li> <li>• Some public comments objected to the “anchor” approach as being outdated and not reflective of current industry structure.</li> </ul>
Number of size standards	The calculated size standards were rounded to one of the predetermined fixed size standards levels. There were eight fixed levels each for receipts-based and employee based standards.	Each NAICS industry is assigned a specific size standard, with a calculated receipts-based standard rounded to the nearest \$500,000 and a calculated employee-based standard rounded to 50 employees (to 25 employees for Wholesale and Retail Trade).	<ul style="list-style-type: none"> <li>• Section 3(a)(8) of the Small Business Act mandates SBA to not limit the number of size standards and to assign an appropriate size standard for each NAICS industry.</li> <li>• Some public comments also raised concerns with the fixed size standards approach.</li> </ul>
Federal contracting factor	Evaluated the small business share of Federal contracts vis-à-vis the small business share of total receipts for each industry with \$100 million or more in Federal contracts annually.	Besides the small business shares of Federal contracts and of total receipts, examines the odds that the small businesses win Federal contracts for each industry with \$20 million or more in Federal contracts annually.	<ul style="list-style-type: none"> <li>• Some public comments were concerned that the methodology does not adequately account for Federal market conditions and recommended that SBA examine barriers for small businesses to enter the Federal market. Including the odds of winning contracts ameliorates the concern.</li> <li>• The \$100 million threshold excludes more than 80 percent of industries from the consideration of the Federal contracting factor. Lowering that to \$20 million almost doubles the number of industries for which the Federal contracting factor will apply.</li> <li>• Expanding the analysis of the Federal contracts also improves the an analysis of the industry’s competitive environment pursuant to section 3(a)(6) of the Small Business Act.</li> </ul>
Industry competition	Was considered as significant factor if the 4-firm concentration ratio was 40 percent or more and 4-firm average formed the basis for the size standard calculation for that factor.	Considers all values of the 4-firm ratio and calculates the size standard based directly on the 4-firm ratio. Industries with a higher (lower) 4-firm ratio are associated with a higher (lower) standard.	<ul style="list-style-type: none"> <li>• Some commenters opposed using the 40 percent threshold and recommended using all values of the 4-firm ratio.</li> <li>• The 4-firm average is highly correlated with the weighted average.</li> </ul>

### Impacts of Changes in the Methodology

To determine how the above changes in the methodology would affect size standards across various industries and sectors, SBA estimated new size standards using both the “anchor” approach and the “percentile” approach for each industry (except those in Sectors 42 and 44-45, and Subsectors 111 and 112). For receipts based size standards, the anchor group consisted of industries with the \$7.5 million size standard, and the higher size standard group included industries with the size standard of \$25 million or higher, with the weighted average size standard of \$33.2 million for the group. Similarly, for employee based size standards the anchor group comprised industries with the 500-employee size standard, and higher size standard group comprised industries with size standard of 1,000 employees or above, with the weighted average size standard of 1,182 employees. These and 20<sup>th</sup> and 80<sup>th</sup> percentile values for receipts-based and employee-based size standards are shown, below, in Table 3, “Reference Size Standards under Anchor and Percentile Approaches.”

**Table 3**  
Reference Size Standards under Anchor and Percentile Approaches

	Anchor Approach		Percentile Approach	
	Anchor level	Higher level	20th percentile	80th percentile
Receipts standard (\$ million)	\$7.5	\$33.2	\$7.5	\$32.5
Employee standard (no. of employees)	500	1,182	500	1,250

Under the anchor approach, we derived the average value of each industry factor for industries in the anchor groups as well as those in the higher size standard groups. In the percentile approach, the 20<sup>th</sup> percentile and 80<sup>th</sup> percentile values were computed for each industry factor. These results are presented, below, in Table 4,

“Industry Factors under Anchor and Percentile Approaches.” As shown in the table, generally, the anchor values are comparable with the 20<sup>th</sup> percentile values and higher level values are comparable with the 80<sup>th</sup> percentile values.

**Table 4**  
Industry Factors under Anchor and Percentile Approaches

	Anchor Approach		Percentile Approach	
	Anchor	Higher level	20th percentile	80th percentile
Industry factors for receipts based size standards, excluding Subsectors 111 and 112				
Simple average receipts size (\$ million)	0.78	7.09	0.83	7.65
Weighted average receipts size (\$ million)	18.07	724.84	19.42	834.75
Average assets size (\$ million)	0.35	4.73	0.34	5.17
4-firm concentration ratio (%)	10.4	34.5	7.9	42.4
Gini coefficient	0.679	0.830	0.686	0.835
Industry factors for employee based size standards, excluding Sectors 42 and 44-45				
Simple average firm size (no. of employees)	33.4	98.2	29.6	122.7
Weighted average firm size (no. of employees)	232.2	1,362.6	251.3	1,581.6
Average assets size (\$ million)	4.82	23.29	3.92	40.62
4-firm concentration ratio (%)	24.8	50.3	24.8	61.7
Gini coefficient	0.770	0.842	0.760	0.853

Under the anchor approach, using the anchor size standard and average size standard for the higher size standard group, SBA computed a size standard for an industry’s characteristic (factor) based on that industry’s position for that factor relative to the average values of the same factor for industries in the anchor and higher size standard groups. Similarly, for the percentile approach, combining the factor value for an industry with the 20<sup>th</sup> and 80<sup>th</sup> percentile values of size standards and industry factors among the industries with the same measure of size standards, SBA computed a size standard supported by each industry factor for each industry. Under the both approaches,



a calculated receipts based size standard was rounded to the nearest \$500,000 and a calculated employee based size standards was rounded to the nearest 50 employees.

With respect to the Federal contracting factor, for each industry averaging \$20 million or more in Federal contracts annually, SBA considered under both approaches the difference between the small business share of total industry receipts and that of Federal contract dollars as well as the estimated odds that small businesses win Federal contracts under the current size standards. Specifically, under the Revised Methodology, the existing size standards would increase by certain percentages when the small business share of total industry receipts exceeds the small business share of total Federal contract dollars by 10 or more percentage points. Those percentage increases, detailed in the Revised Methodology, to size standards generally reflect receipts and employee levels needed to bring the small business share of Federal contracts at par with the small business share of industry receipts. If the odds that small businesses win Federal contracts for in an industry are found to be significantly lower than one, the results would support an increase to that industry's current size standard. Otherwise, the results would support the existing size standard.

The results were generally similar between the two approaches in terms of changes to the existing size standards, with size standards increasing for some industries and decreasing for others under both approaches. Most impacted sector was construction, with a majority of industries experiencing decreases to the current size standard. Overall, the changes to size standards as the result of the changes in the methodology, if adopted, would have a minimal impact on number businesses that qualify as small under the existing size standards. Excluding NAICS Sectors 42 and 44-45 and Subsectors 111 and

112, 97.73 percent of businesses would qualify as small under the new calculated size standards using the “anchor” approach vs. 97.68 percent qualifying under the “percentile” approach in the Revised Methodology. Under the current size standards 97.72 percent of businesses are classified as small.

### **Alternative Size Standards Methodologies Considered**

The Revised Methodology presents the current size standards methodology employed by SBA. Certainly other methodologies may be developed by applying different assumptions, data sources, and objectives. Over the years, SBA has refined its methodology within a consistent conceptual framework based on the analysis of industry and relevant program data. Several alternative methodologies have been suggested to SBA. In critiquing these, SBA has continued to believe that its historical methodology is sound and adequate because it has resulted in size standards that have been widely accepted by the public and found to be effective in providing Federal assistance to small businesses. Below is a brief description and evaluation of four alternative methodologies suggested to SBA.

#### Financial Performance Analysis

Industry and financial analysts assess the economic viability of businesses using various financial performance indicators, such as return to capital (assets), gross margins, net worth, *etc.* Several private organizations and government agencies aggregate financial data at the firm level to derive the corresponding data at the industry level. Pursuant to the Small Business Act aimed at assisting businesses that are competitively

disadvantaged, financial performance indicators may provide an alternative basis for developing small business size standards.<sup>1</sup>

This approach may provide a basis for identifying businesses, which, due to their size, may be underperforming relative to established industry norms. This, in turn, would form a basis for establishing size standard levels that can target businesses that are in need of Federal assistance.

The major disadvantage of the financial performance analysis approach is, however, the lack of robust and consistent data across industries for several reasons. First, financial data are not available for all industries at the 6-digit NAICS level, especially the distribution of businesses by size. Second, data at the industry level or by size class may be based only on a limited sample of businesses. Third, financial data are also likely to be riddled with measurement errors and accounting holes. These problems as well as concerns related to how businesses are classified in an industry and the treatment of affiliates may limit the applicability of available financial data to size standards analysis. More importantly, there is not necessarily a robust correlation between financial performance measures and size of a business. For example, during economic downturns even very large businesses may perform very poorly in terms of financial indicators, thereby potentially qualifying them as small businesses under size standards based on financial measures.

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<sup>1</sup> See Jim Blum (1991) for evaluation of financial performance analysis as an alternative tool for establishing size standards. Jim was a MBA intern under Gary Jackson, Director of Size Standards.

Given above problems with financial data and possibilities of very large businesses of being qualified as small based on financial indicators, SBA has determined that a financial performance analysis alone is not applicable to developing small business size standards. However, SBA will explore if certain financial indicators can be incorporated into the existing size standards methodology as additional factors.

#### Size Standards Based on Program Objectives

Federal contracting and some SBA financial programs have established specific objectives (targets) in providing assistance to small businesses. Some industrial economists suggest that varying size standards may serve as a tool in ensuring that small businesses are receiving the targeted level of Federal assistance.<sup>2</sup>

The advantage of this approach is that SBA and other Federal agencies can identify and estimate gaps between their predetermined objectives and current levels of attainment for an individual industry or a group of industries. Based on these gaps and the expected impacts of changes in current levels of size standards on program objectives, revised levels of size standards can be established. If an industry's gap in attainment of an objective is positive, its size standard can be reduced. Similarly, if the gap is negative, the level of associated size standard can be increased. Through repeated (iterative) adjustments of size standards this way would result in higher degrees of attainment of various objectives and produce uniform levels of size standards for similar groups of industries.

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<sup>2</sup> CONSAD. Proposed Options for Settings Business Size Standards.

There are several serious flaws with this approach. First, the size standard becomes a function of a size of business supporting some predetermined levels of program objectives instead of identifying businesses that are, due to their size and other reasons, in a competitively disadvantaged position and need Federal assistance. Second, the approach generates fluctuating size standards based on past trends of small business assistance as opposed to those based on current needs of small businesses. Third, this approach assumes that the decision to approve a loan or award a contract is based primarily on the size of a business size rather than its credit worthiness or capabilities to execute Federal contracts. Fourth, the necessary data to evaluate the size standards are not available on a timely basis. For example, detailed industry data are available only once every five years. Similarly, verified Federal contracting data usually have least one year time lag. Finally, this approach would require establishing size standards on a program-by-program basis, thereby making size standards more complex and confusing to users.

For the above reasons, SBA does not apply this approach for establishing size standards. The Agency feels that a size standards methodology must focus on identifying businesses that are in need of assistance as opposed to what level of assistance is provided under a particular program. SBA considers the small business participation in Federal contracting and SBA financial programs as one of the five factors in its current methodology. The frequent adjustment of size standards under this approach would create a high level of uncertainty among small businesses and overwhelm the regulatory process. This approach would be more appropriate as a program evaluation tool rather than a size standards methodology.

### Size Standards Based on General and Administrative Workforce

A size standard for an industry may also be developed by examining the level of general and administrative workforce needed for a business to be competitive and calculating the amount of revenues at that level of workforce. General and administrative workers do not directly contribute to revenues of a business and must be supported by revenues generated from the goods and services produced. Total revenues needed to support the general and administrative workforce for a competitive business can be calculated based on average overhead rates, general and administrative compensation, fess, direct labor costs, materials, and subcontractor costs for a relevant industry.

This approach takes into consideration at what size a business becomes competitive. It attempts to identify the size of business that has overcome the competitive disadvantages associated with size.

The primary disadvantage of this approach is its reliance on an assumption that there exists a level of general and administrative workforce for a business to be competitive. There are no data sources that objectively provide that information. This approach also suffers from several methodological flaws, the most significant of which is inferring specific business level experience to the industry level. The type of data necessary to perform the calculation may be biased towards large businesses that are more likely to report such data.

SBA does not use this approach because of the degree of arbitrariness of the underlying assumption. Moreover, this approach is likely to result in a much higher level of size standard, while an industry comprises a large number of competitive businesses below that level.

### Size Standards Based on Qualitative Characteristics

While most size standards methodologies tend to define a small business in quantitative terms (*e.g.*, the number of employees, annual receipts, amount of assets, *etc.*), some business analysts and industry economists have also attempted to define a small business in qualitative terms. Under this approach, certain characteristics are used to differentiate businesses that are small from those that are not small. Some of the most commonly cited characteristics in the literature include the management and ownership structure of the business, control and decision making process, and sources of financing. Specifically, small businesses tend to share the following characteristics: they are independently owned and operated; they are closely controlled by owners/managers who also contribute most of the operating capital; and principal decision making functions rest with owners/managers.<sup>3</sup>

This approach resolves the inherent arbitrariness associated a strict numerical definition. It also focuses on the notion of what factors distinguish a business as small relative to a competitively viable business operation.

The most obvious disadvantage of this approach rests with the ability of SBA to verify the small business status. An on-site review of the business would have to be conducted to determine small business status. Also, businesses would not have definitive criteria to quickly assess their small business status. The difficulty of obtaining a consensus on what characteristics to examine and their interpretation would render the

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<sup>3</sup> See Holmes and Gibson (2001) for a detailed analysis of various quantitative and qualitative definitions of small business.

implementation of a qualitative small business size standard more contentious than a numerical approach.

The requirement to establish a definitive and easily verifiable small business size standard precludes this approach as an alternative size standards methodology for SBA.

### **Request for Comments**

In addition to comments on the various policy issues, SBA welcomes comments from the public on a number of other issues concerning its size standards methodology.

Specifically, SBA invites feedback and suggestions on the following:

- Should SBA establish size standards that are higher than industry's entry-level business size? SBA generally sets size standards higher than the entry-level business size to enable small businesses to compete against others of their size and (often) considerably larger businesses for Federal contracts set aside for small businesses. It is important that small businesses be able to apply for and be eligible for SBA's various business development programs that have additional requirements, such as a minimum number of years in business to qualify for its 8(a) Business Development Program. This precludes setting size standards at too low a level or at the entry-level size. Additionally, establishing size standards at the industry entry-level firm size would cause small businesses to outgrow their eligibility very quickly, thereby lacking sufficient cushion or experience to succeed outside of the small business market and leading to their demise. Finally, size standards must be above the entry-level size to ensure small businesses have necessary resources and capabilities to be able to perform and meet Federal government contracting requirements.



- Should size standards vary from program to program? In other words, should SBA establish one set of standards for SBA loan programs, another for Federal procurement, or yet another for other Federal programs? SBA had, in the 1980s, established different size standards for different programs. The result had been that some firms were small for some programs and large for others. Such size standards were very confusing to users and caused unnecessary and unwanted complexity in their application. The statutory guidance encourages an industry by industry analysis and not a program-by-program analysis when developing small business size definitions. While the characteristics and needs of a particular SBA program may necessitate the deviation from the uniform size standards, the Agency will continue its general policy of favoring one set of size standards for all programs. However, SBA has established 13 special size standards for some activities within certain industries for Federal government purposes. Similarly, for industries in Wholesale Trade and Retail Trade, SBA has established industry specific size standards for SBA's loan and Federal nonprocurement programs and a common 500-employee size standard for Federal procurement under the nonmanufacturer rule. Additionally, for SBA's 7(a) and 504 loan programs businesses can qualify either based on industry specific size standards for their primary industries or based a tangible net worth and net income based alternative size standard.
- Should size standards apply nationally or should they vary geographically? The data SBA obtains from the Economic Census are national data. While the Economic Census does publish a Geographic Series of the data, application of

those data to evaluating and establishing size standards would be cumbersome and time consuming at best, resulting in a very complex set of size standards that would likely be unusable. For example, in Federal contracting, how would a contracting officer set the size standard on a contracting opportunity? Would it depend on the contracting officer's location? On the location of the Agency's headquarters? On the place of delivery of the product or service? What about multiple delivery locations? On the location of the prospective contractor? On the location of the prospective contractor's headquarters? What if that were not in the U.S.? What about subcontractors, since size standards apply to their contracts as well? The same questions could be asked about them, which would affect a prime contractor's ability to bid. Would this encourage firms to relocate based upon perceived favorable size standards? That would defeat the purpose behind geographic distinctions. The undue complexity and resulting confusion would render geographic size standards unusable, for all practical purposes.

- Should there be a single basis for size standards – *i.e.*, should SBA apply the number of employees, receipts, or some other basis to establish its size standards for all industries? SBA considered having a single basis for its size standards in the past. In 2004, SBA proposed to establish all size standards based on number of employees. This proposal received mixed comments from the public SBA withdrew the proposal. Commenters viewed either that either receipts was a more suitable measure of size for many industries or that the proposed employment levels were too low.

- Should there be a ceiling beyond which a business concern cannot be considered as small? In other words, should there be a maximum size standard? SBA has not increased its employee based standards beyond the 1,500-employee level. However, receipts based size standards have gradually increased over time and the highest standard stands at \$38.5 million today. This is a policy decision that the Agency should make – is there a size beyond which a business is not small?
- Should there be a fixed number of size standard ranges or “bands” as SBA applied for the recently completed comprehensive size standards review? This was one of the issues to which SBA sought comments in the recent review and generally received favorable comments from the public. However, NDAA 2013 amended the statute requiring SBA not to limit the number of size standards and assign the appropriate size standard to each NAICS industry. Similarly, should SBA establish a common size standard for related industries even though the data may support different size standards for individual industries?
- Should SBA consider adjusting employee based size standards for labor productivity growth or increased automation? Just as firms in industries with receipts based standards may lose small business eligibility due to inflation, firms in industries with employee based standards may gain eligibility due to improvement in labor productivity. While the original \$1 million receipts based size standard has now increased to \$7.5 million due to adjustments for inflation, the 500-employee manufacturing size standard set at the inception of SBA has remained the same.

- Should SBA consider lowering its size standards? SBA receives periodic comments from the public that its standards are too high in certain industries or for certain types of Federal contracting opportunities. The comments generally concern the competitive edge that large small businesses have over the “truly small business” (a phrase heard frequently from commentators). This has always been a challenging issue, one that SBA has had to deal with over the years. SBA’s size standards appear large to the smallest of small businesses while larger small businesses often request even higher size standards. In the recently completed comprehensive size standards review, in view of the economic climate following the 2008-2009 recession and various measures Federal Government implemented to stimulate employment and economic growth, SBA decided to not lower size standards even if the data supported lowering them. This issue is partly tied to Federal procurement trends of contracts getting larger over time, and they are often out of the reach of the “truly small businesses.”
- Should SBA size standards be specific, *i.e.*, to the precise dollar calculated based on the data and information it evaluates? Or should SBA recognize that there are other factors that go into establishing size standards, such as the fact that the data SBA evaluates is not static, industries change over the years, and even within a given year.
- Should SBA round off its calculated size standards for the various industries? If so, should SBA always round up? To what level? If not, what about those industries that do not get increases in size standards when others are? What should be the cut-off point for rounding either one way or the other?

- SBA’s new percentile based approach to evaluating industry characteristics, which will replace the “anchor” size standards approach the Agency used in the past;
- Alternative methodologies for determining small business size standards;
- How SBA’s size standards impact competition in general and within a specific industry;
- Alternative or additional factors that SBA should consider;
- Whether SBA's approach to small business size standards makes sense in the current economic environment;
- Whether there are gaps in SBA's methodology because of the lack of comprehensive industry and Federal market data; and
- Alternative or other factors or data sources SBA should consider when establishing, reviewing, or modifying size standards.

SBA encourages the public to review and comment on the Revised Methodology available at [www.sba.gov/size](http://www.sba.gov/size). SBA will thoroughly evaluate and consider all comments and suggestions when finalizing the Revising Methodology, which the Agency will apply in the forthcoming, second five-five year review of size standards as required by the Jobs Act.

Dated:

Linda M. McMahon,  
Administrator.